

March 15, 2004

Honorable Mayor and Members of the  
City Commission  
City of Muskegon  
Muskegon, Michigan 49443

Ladies and Gentlemen:

We are pleased to present to you the Comprehensive Annual Financial Report (CAFR) for the City of Muskegon, Michigan, for the year ended December 31, 2003, in accordance with the requirements of state law. The financial statements are presented in conformity with generally accepted accounting principles (GAAP), and audited in accordance with generally accepted auditing standards by a firm of licensed certified public accountants. This annual report is formatted to comply with the financial reporting model developed by the Government Accounting Standards Board (GASB) Statement 34.

GAAP requires that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement MD&A and should be read in conjunction with the financial statements. The City of Muskegon's MD&A can be found immediately following the independent auditor's report.

The City has elected not to report historic infrastructure or related depreciation costs in this report as allowed by GASB 34. GASB 34 requires that this information be included in the City's CAFR by the year ending December 31, 2007; the City, however, intends to report this information in its 2004 CAFR.

The Comprehensive Annual Financial Report is prepared by the City's Finance Department and responsibility for both the accuracy of the data presented and the completeness and fairness of the presentation, including all disclosures, rests with the City. We believe the data as presented is accurate in all material respects; that it is presented in a manner designed to set forth fairly the financial position and results of operation of the City as measured by the financial activity of its various funds and component units; and that all disclosures necessary to enable the reader to gain the maximum understanding of the City's finances have been included. Hoffman, Steensma & Plamondon, P.L.C., Certified Public Accountants, performed the independent audit of all accounts of the City as required by state law, and their report

and unqualified opinion is presented as the first component of the financial section of this report.

## **THE CITY AND THE REGION**

The City of Muskegon is located in Western Michigan on the shores of Lake Michigan. The City covers eighteen square miles and, with a population of 40,105, is the largest city on the Eastern Shore of Lake Michigan. The City is located within the County of Muskegon and is part of the vibrant Grand Rapids-Muskegon-Holland metropolitan statistical area (MSA):

- According to Site Selection magazine's 2001 annual nationwide survey of corporate locations, the Grand Rapids-Muskegon-Holland MSA ranked seventh in the country with 223 new and expanded facilities.
- With West Michigan's diverse industrial sector and excellent intergovernmental cooperation, the area has ranked in the top 30 out of 315 metropolitan communities in Industry Week's World Class Community annual survey for five consecutive years.
- The Muskegon-Grand Rapids-Holland area finished 13th in a national ranking of the 50 best large metropolitan areas for starting and growing a business. The survey produced annually by Cognetics Inc., a Waltham, Massachusetts-based economics research firm, compares the business climates in communities by analyzing significant new business starts and looking at the growth rate of young businesses.
- West Michigan is a fun place to be! Places Rated Almanac ranked the area No. 3 in the fun and recreation category.
- Muskegon's Pere Marquette beach has been nationally recognized as one of the best beaches in the nation by USA Today and was the only beach in the state to receive and maintain the Blue Wave Certification by the Clean Beaches Council. The Blue Wave certification identifies the nation's cleanest, safest and most environmentally well-managed beaches. In April 2003, The Detroit News voted Muskegon's Beaches #1 as the "Best Place to Run Sand Between Your Toes".
- Muskegon has become a cultural hub for West Michigan with many museums and live performances. The Muskegon Museum of Art has the third best art collection in the Midwest, and the Muskegon County Museum provides insight into the area's history. The former residences of Muskegon's lumber barons, Charles H. Hackley and Thomas Hume, proudly display the glory of the Victorian ages. The Fire Barn Museum takes visitors back to a 1890s Muskegon Fire Station. The West Shore Symphony and Muskegon Civic Theater bring the stage of The Frauenthal Center for the Performing Arts to life throughout the year. The Great Lakes Naval Memorial and Museum allows visitors to step back in time and tour the USS Silversides, a surviving World War II submarine.

The City operates under a Commission-Manager form of government and provides the full range of traditional municipal services. These include police and fire protection,

parks and recreation activities, public works operations, water and sewer services, parking facilities, solid waste collection, community development and general administrative support services. The City also provides treated water to a number of surrounding communities on a wholesale basis.

### **COMPONENT UNITS**

The City has one blended component unit, the Muskegon Building Authority/Tax Increment Finance Authority, a separate legal entity that uses the proceeds of its tax-exempt bonds to finance construction of certain general fixed assets for the City. The bonds are secured by lease agreement with the City and retired from lease payments made by the City.

The City also has discretely presented component units. These entities are discretely presented in the financial statements as the governing boards of the component units are substantially the same as the City's governing board:

- The Downtown Development Authority for redevelopment activities in the City's downtown area. Bonds are repaid through tax increment revenues generated by development within the Authority's boundaries.
- The Local Development Finance Authority issues bonds for development activities in the City's industrial park and high-tech park areas. Bonds are repaid through tax increment revenues generated by development within the Authority's boundaries. The City has created three separate local development finance authority districts under the aegis of the Local Development Finance Authority (LDFA).

### **LOCAL ECONOMIC CONDITION AND OUTLOOK**

Muskegon is fortunate to have a diverse local economy. The manufacturing sector is strong in the areas of aerospace, chemicals, plastics, metals and castings, office furniture and automotive parts. The City of Muskegon also benefits from being home to large government, corrections, healthcare, and educational employers. The local income tax withholdings remitted by these employers help provide stability to City finances in times of economic weakness. According to the W.E. Upjohn Institute, employment growth for Muskegon County in 2003 was 0.2% (measured by place of employment) and 1.8% (measured by place of residence). The employment growth rate is projected to be -0.1% in 2004 rebounding to 0.9% in 2005.

### **MAJOR INITIATIVES AND ACCOMPLISHMENTS**

Among the City's major initiatives and accomplishments in 2003 were the following:

- Lake Express LLC announced new high-speed cross-lake ferry service linking Muskegon with Milwaukee, Wisconsin was announced. Service will begin in June 2004 with three roundtrip lake crossings each day. The City assisted in this project by committing to provide parking and certain site improvements at an estimated

cost of \$1.2 million. Conservative projections show that at least 100,000 visitors will disembark the ferry in Muskegon each season.

- Work was completed on infrastructure improvements for “Edison Landing” a state-designated “Smartzone” on Muskegon’s downtown lakefront. The Muskegon Smartzone initiative is a joint venture between the Michigan Economic Development Corporation, Grand Valley State University (GVSU), the City of Muskegon, and private developers. The site is anchored by GVSU’s *Michigan Alternate Resource Energy Center (MAREC)* which was opened in November 2003. This facility focuses academic and private sector resources on the development and commercialization of alternate energy sources. The City, through its Local Development Finance Authority, assisted in this project through issuance of \$4.725 million of bonds for construction of MAREC. When complete, the Muskegon Lakeshore Smartzone will include premier office space, retail, and residential living.
- Work continued on construction of the \$12 million extension of Shoreline Drive. When completed in July 2004, the new road will be designated as *Business US-31* and will route 23,000 vehicles along the city’s downtown waterfront and the previously mentioned Edison Landing project each day.
- Demolition work was started on the former Downtown Mall property. When cleared, this 21-acre site will be developed as mixed-use residential and commercial site. The Downtown Muskegon Development Corporation is spearheading the development and the City is assisting through the granting of a tax-free “renaissance zone” status and through limited financial participation in the construction of necessary infrastructure improvements.
- Work began on renovation of a former office equipment manufacturing plant into loft-style apartment/condominium units. The plant comprises nearly one million square feet of space and is well suited for residential living being located directly across from the downtown municipal marina and waterfront.

## **OTHER INFORMATION**

### **INTERNAL ACCOUNTING CONTROLS**

The City’s management is responsible for establishing and maintaining an internal control structure that is designed to ensure adequate protection of the City’s assets from loss, theft, or misuse, and adequate accounting data to allow for preparation of financial statements in conformity with generally accepted accounting principles. The internal control structure is designed to provide reasonable, but not absolute assurance that these objectives are met. The concept of reasonable assurance recognizes that (1) the costs of a control should not exceed the benefits likely to be derived; and (2) the valuation of costs and benefits requires estimates and judgments by management.

All internal control evaluations occur within the above framework. We believe that the City's internal accounting controls adequately safeguard assets and provide reasonable assurances of proper recording of financial transactions. Also, in conjunction with this year's audit, the City's independent auditors implemented new procedures and tests in accordance with Statement on Auditing Standards (SAS) No. 99 *Consideration of Fraud in a Financial Statement Audit*.

## BUDGETARY CONTROL

Budgetary control is maintained through an annual budget resolution passed by the City Commission. Budgetary control at the functional level is maintained by review of estimated expenditures prior to making purchases. Purchases that result in over expenditure of budget levels are not made until additional appropriations or budget changes are processed to make funds available.

Encumbrances are not recorded in the City's funds. The City does, however, utilize an informal monitoring system to facilitate budgetary control over proposed purchases. Essentially, this system entails the use of on-line budgetary information that details year-to-date "actual versus budgeted" expenditure comparisons by budget category. This information is accessible to appropriate personnel to enable them to ascertain the budget status of an expenditure category prior to authorizing additional purchases.

## DEBT ADMINISTRATION

At December 31, 2003, the total of City bonds and contractual debt outstanding (including discretely presented component unit debt) was \$31,778,823 as compared to \$34,024,914 at December 31, 2002. During the year, the Local Development Finance Authority (a component unit) called \$725,000 limited tax obligation bonds with available cash on hand. Also in 2003, the City issued \$1.575 million of capital improvement bonds for purposes of financing sidewalk improvements. During the year, Standard & Poor's affirmed the City's general obligation debt rating of **A**.

## CASH MANAGEMENT AND INVESTMENTS

Temporarily idle cash from the City's various funds is invested through management of a common pooled cash and investments system. Maturity of investments are timed to meet the City's cash needs. Investment instruments generally consisted of U.S. Treasury Bills and Notes, government agency securities, high quality commercial paper and liquid money-market funds. Daily liquidity needs are managed by investments in money-market funds of all cash not needed in the common checking account to cover checks and other debits presented to the bank for payment that day. The City has contracted with MBIA Municipal Investors Service Corporation to provide full-time, non-discretionary management of the City's operating funds portfolio.

## PENSIONS AND OTHER POST-EMPLOYMENT BENEFITS

The City of Muskegon sponsors two locally-administered defined benefit pension programs: the *Police and Fire Retirement System* for uniformed police and fire personnel and the *General Employees' Retirement System* for all other full-time employees. Each year an independent actuary engaged by the respective pension boards calculates the annual contributions that the city must make to ensure the retirement systems are able to meet current and future obligations. Both of the City's retirement systems are more than fifty years old and the City has a longstanding policy of fully funding each year's contribution requirements as determined by the actuary.

The City also provides post-retirement health benefits for retirees and their dependents. Since 1987, the City has also had an actuarial valuation of its post employment healthcare obligation performed each year and has followed a program of prefunding the obligation in the same manner as the pension obligations. GAAP does not currently require governments to report a liability in the financial statements in connection with an employer's obligation to provide these benefits.

## RISK MANAGEMENT

During 2003, the City continued participation in the Michigan Municipal Risk Management Authority (MMRMA), an intergovernmental cooperative self-insurance program. The MMRMA offers secure liability and property insurance coverage with premium stability and broad coverage at a competitive price. The City is insured up to \$15 million with a \$75,000 deductible per occurrence for general, auto, public official and law enforcement liability. Since the City began participating in the MMRMA program in March 1986, total incurred losses (i.e. exclusive of reinsurance recoveries) have been \$7,441,437.

## SINGLE AUDIT

The City is required to have an annual single audit in conformity with the provisions of the Single Audit Act Amendments of 1996 and U.S. Office of Management and Budget Circular A-133, "Audits of State, Local Governments and Non-Profit Organizations". Information related to the single audit, including the schedule of federal awards, findings and questioned costs, and auditors' reports on internal control over financial reporting and compliance with certain laws, regulations and grants are published in a separate single audit report. The financial activities related to the single audit requirements, such as the Community Development Block Grant Program, are included in this financial report.

## AWARDS

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the City of Muskegon for its Comprehensive Annual Financial Report for the fiscal year ended December 31, 2002. This was the eighteenth consecutive year that the City has received this prestigious award. In order to be awarded a Certificate of

Achievement, a governmental unit must publish an easily readable and efficiently organized Comprehensive Annual Financial Report, whose contents conform to program standards. Such reports must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe our current report continues to conform to the Certificate of Achievement Program requirements, and we are submitting it to the GFOA to determine its eligibility for another certificate.

#### ACKNOWLEDGEMENTS

The preparation of this report could not be accomplished without the dedicated and efficient services of the staff of the Financial Services Division and the Muskegon County Print Shop. We would also like to thank the members of the City Commission for their continued interest and support in conducting the financial affairs of the City in a responsible and progressive manner and for their tireless efforts in working for the betterment of the Muskegon community.

Respectfully submitted,

Bryon L. Mazade  
City Manager

Timothy J. Paul  
Director of Finance









